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E.O. 12958: DECL: 02/04/2018  
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SUBJECT: ARGENTINA PERSPECTIVES

Classified By: Ambassador E. Anthony Wayne for reasons (B) and (D).

11. (SBU) Summary: As part of outreach efforts during recent friction in U.S.-Argentine relations, Ambassador held one-on-one discussions with key players on the Argentine scene. In each, he explained the U.S. perspective on discord over the Miami court case and on bilateral relations. Interlocutors expressed strong support for the U.S. position and offered to help quietly. Almost to a person, they said the GoA's overreaction reflected a limited understanding of the U.S. and things international, the very small circle of decision-makers for key issues, and the penchant for the Kirchners to respond aggressively to perceived challenges and make up afterwards. Interlocutors anticipated the GoA's reconciliation efforts with the USG, noting the Kirchner regime's need for U.S. and international investment/financing and the fact that, while anti-Americanism plays well in Argentina, serious conflict with the United States does not.

12. (SBU) Interlocutors were also fairly united in their views on the challenges facing the government: controlling inflation and wages and dealing with public security concerns related to rampant street crime. Many noted that the new government has yet to break out of the short-term framework for policy-making which characterized Nestor Kirchner's government and suggested that Cristina Fernandez de Kirchner (CFK) had yet to demonstrate that she will govern in a manner

distinct from that of her husband. End Summary.

13. (SBU) The following are highlights of individual conversations over the past three weeks. Topics covered include GOA decision-making style, economic policy making, inflation, salary negotiations, investment policy, public security challenges, anti-Americanism, corruption, oil and energy policy, and regional security concerns.

Bank President

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14. (SBU) Clarisa Lifsic is President of the Banco Hipotecario, Argentina's second largest bank in terms of net worth. She has an MBA from MIT and represents private shareholders in this formerly state-owned mortgage bank. Private shareholders control the majority of seats on the board, but various public entities still control over 50% of Hipotecario's stock following its "de-nationalization" in 1997. While the bank used to specialize in mortgages, it is now a full service bank and has been expanding rapidly in recent years.

15. (C) She sees the main challenge to the Argentine economy and the banking system as getting inflation under control. The GoA's interventionist anti-inflation policy, including freezes in public utility tariffs and "voluntary" price stabilization agreements on a sizeable basket of consumer goods, has just hidden a very serious problem.

16. (C) The government has displayed little understanding of how to expand credit markets for medium- or long-term loans. Just before the elections, the government got banks to pledge to issue small enterprise and mortgage loans at less than the cost of money at that time. The banks signed because the head of the Banking Association (see para. 12) assured them that the government just wanted the headlines and would never check to see if the loans were issued. The government has no long-term vision or plan about generating a mortgage market,

for example. You don't do that by telling banks they have to make loans at a loss, she said. You create policy structures and make funds available in the way Mexico did to begin expanding home mortgages.

17. (C) The appointed government members of the Banco Hipotecario Board of Directors have been weak. The last two were friends of former Finance Minister Felisa Miceli's siblings. One was an architect, who knew nothing about banking, and the other was an accountant, but he still asked where the mortgages were kept on his initial tour of the bank. Much time had to be spent educating them both on basics and keeping them informed of what issues and topics meant. Similarly, the lack of coordination and clear lines of responsibility within the government mean that a great deal of time has to be spent going individually to each actor in the government who might influence the bank's policy to brief them on new policies or strategic decisions by the bank.

It is a very time-consuming process.

18. (C) One of the great failings of GOA policy has been its very short-term focus. There has been hope that CFK may change that. She asked a number of individual economists and economic players to write longer term strategy papers for her. She has also told at least one person that she intends to create a committee charged with developing a longer term economic vision for Argentina. So far, however, there have not been any clear signs of more focus on the longer term. There is also no clear sign so far that the government will implement the "social pact" between labor, business and the government which CFK discussed in her electoral campaign.

International Banker and Financier

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19. (SBU) Guillermo "Willy" Stanley is a board member of Macro Bausud, one of Argentina's largest banks, former President of Citibank Argentina, and Director of D&G, a

consulting and investment firm that owns Havanna, a very successful Argentine cookie and coffee bar company. Stanley noted that his companies have been prospering with Argentina's economic growth. Havanna sales have grown 7% over the past year. It now has 30 stores in other parts of Latin America and hopes to open a store in the United States.

Macro Bansud's deposit base has been growing steadily in recent years, loans are booming, and the bank has been able to borrow significant amounts at excellent rates in Europe over the past year.

¶10. (C) Inflation is the biggest challenge facing the government. The inept price control policies of Commerce Secretary Guillermo Moreno have made the problem much more

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serious than it needed to be. By destroying the credibility of the national statistics agency, INDEC, and by using offensive pressure tactics to try to control prices, the government has raised inflationary expectations for most economic actors. Rather than what easily could have been inflation hovering around 13%, now most sectors have (self-fulfilling) expectations that inflation will be 20-25%.

This has repercussions across the economic spectrum as recent union claims for wage increases demonstrate.

¶11. (C) The government's repeated focus on the short-term is also taking its toll. There had been hope that CFK would bring about a change in her husband's focus on the immediate, but decisions are still being made by the same small group and with no evident shift from the near-term political motivation for most decisions.

Banking Association President

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¶12. (SBU) Jorge Brito is president of Banco Macro, Argentina's largest bank by several measures, and president of the association of Argentine-owned private banks, ADEBA.

Macro has over 7,000 employees and 440 branches operating in many provinces. It has enjoyed over 20 consecutive profitable quarters.

¶13. (C) In Brito's view, Argentina's economy is well placed to weather the current international turmoil, but the domestic banking sector will still be squeezed by the higher cost of international capital, as money retreats from perceived risk. The government needs to start letting prices rise on energy and key services and start to give more signals to encourage investment. The key in the near term will be where salary negotiations end up. If they end up granting higher than 20% raises, for example, that will seriously fuel inflationary expectations and produce dangerous effects throughout the economy. If the final set of raises average less than 20%, the effects will probably be manageable. The government needs to adopt a new set of policies for tackling inflation. The price limits and other controls were supposed to be in place only for the short term, but clearly, after more than a year in practice, they are not working.

¶14. (C) Brito observed that the banking sector is growing well, with Banco Macro having a 40% growth in loans last year for example. But the key to continued domestic economic growth is job creation, and much of that will only come if new domestic investment, especially by SMEs, is affordable. The government has started again to urge private banks to make loans at low interest rates, but how, he asked rhetorically, can a bank make a five year loan at 7% if it has to give 10% to get 60 day deposits? Only if the government finds a way to offer a guarantee or something like a rate subsidy, can private banks lower rates. So far, he said, the government has not come up with workable ideas or mechanisms.

¶15. (C) Brito noted that Argentina still suffers from having a large part of the money flow in the economy taking place in the informal system. Only about 65% of the money flows in the formal system. The rest is off the books, and many

entrepreneurs are fighting hard to keep it that way, as it allows them to save about 25% that would otherwise go into retirement and health benefit payments. The rural economy also has much of its transactions taking place through informal, untaxed transactions, he said. Brito added that he and his association looked forward to working further with the USG on better controls for money laundering and against terrorist finance.

Political Pollster and Professor

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¶16. (SBU) Manuel Mora Y Araujo is currently Professor in the Masters in Journalism program at the Di Tella University and in the Masters in Political Science program at CEMA University. He is also the Director of the International Center of Public Opinion of Torcuato Di Tella Institute and director of the local polling firm IPSOS, among many other activities.

¶17. (SBU) He argues that the government will be judged by how well it handles the problems of inflation and public security. People are deciding how happy they are depending on how much money they have to spend in their pockets, what they can buy with it, and how safe they feel carrying their money around. CFK's poll numbers have improved since her inauguration, in part because people feel they are doing well in their personal lives and give her the benefit of the doubt at the moment.

¶18. (C) CFK's overreaction to the U.S. court case and Nestor Kirchner's ill-fated trip to Colombia as "guarantor" of a hostage release doesn't weigh heavily, because most of the Argentine public do not care that much about foreign affairs.

Plus, in the case of the United States, playing the anti-American card pays off initially. Governments have to be careful, however, as the population doesn't like being in conflict with the United States - a strange (but, from our perspective, salutary) counterpoint to the anti-Americanism.

Thus, in this case as in many past ones, the best U.S. response to an anti-American outburst by an Argentine government is not to fuel the fire but just to keep calmly explaining the U.S. point of view.

¶19. (C) CFK intellectually knows the value of having a long-term vision and implementing it, but she is short-term in her political outlook and practice, he said. She and her husband share that outlook, but she is still more interested in exploring new concepts and new countries than her husband. That might be an advantage.

¶20. (C) It is far from clear that CFK will implement the "social pact" that she talked about between labor, capital, and government over how to keep the economy growing without disruption for the years ahead, according to Mora Y Araujo. We have not heard much of the concept from CFK and getting something like that done will take a great deal of political effort and capital - no signs of plans to do that so far.

¶21. (SBU) Di Tella University's 50th Anniversary: Many events are planned for this year. The university would like to coordinate on some joint work with the Embassy on bringing in speakers and working with U.S. universities, for example.

German Ambassador  
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¶22. (C) Regarding the Paris Club debt, German Ambassador Wolf Rolf Schumacher said that until the crisis with the USG, the Germans were getting strong messages that the new GoA wanted to move pretty rapidly on solving the debt, but since early December the GoA has gone silent. The Germans think this is because the GoA knows that the USG will be an obstacle unless relations improve. They expect the GOA to move ahead if relations with the U.S. improve.

¶23. (C) Many German companies are doing quite well selling into this market, but most are not making big new

investments. Volkswagen is an exception. Its local CEO (and former Austrian Chancellor) Victor Klima has gone out of his way to court CFK, using his connections in Europe with good results. Siemens has found the Argentines eager to purchase its turbines. As far as the Embassy can tell, all of the energy deals are on the up and up. However, corruption is widespread. One German CEO went into see Planning Minister De Vido to complain that one of his deputies had solicited a bribe and the CEO had refused. De Vido reportedly took no interest in getting the name of the offending official but instead recommended the CEO film and record the next bribe solicitation.

¶24. (SBU) Germany's Max Planck Institute has decided to build its own regional center in Buenos Aires adjoining the new GoA science center. This will be only the second overseas institute location for Germany, and Buenos Aires was chosen because of the consistently high quality of students and researchers who travel from Argentina for training and scholarships at the Institute in Germany.

¶25. (C) The German Ambassador noted that it had been a big challenge to get Chancellor Merkel to agree to meet with CFK several months ago during CFK's visit to Germany, given the reputation of the Kirchner government in Germany. But Merkel agreed to do so in part because of signs that CFK might bring about some changes. However, so far there are no real changes evident. Decisions are still made by the same small group. The clash with the United States, he opined, shows that advice from outside that group (e.g., from the Foreign Minister) is not sought or heeded. The focus is still on the short-term and political, rather than on medium- and longer-term goals. Relations with other countries are still not highly valued, even if CFK has a personal interest in travel and in meeting other leaders. It is not an impressive start.



¶26. (C) Mario Montoto is involved in defense and security industries, publishes a monthly magazine on defense and international affairs issues called DEF, and is an ex-advisor to the head of the Montonero guerrillas. He is now very pro-U.S. and does business with Israel. Montoto says the crisis with the USG is rooted in the limited perspectives of the key decision-makers. For example, the Vatican is refusing to accept the GoA nominee for ambassador, former Justice Minister Irribarne, because he is a divorced and remarried Catholic. The key decision-makers did not consider that a 2000-year-old institution that has opposition to divorce for Catholics like Irribarne as one of its key principles might have a problem with this nominee. In the case of the Miami arrests, it took the key GoA figures a while to figure out that these were not orchestrated by the USG. Montoto said he had raised this "'mistake'" with the head of Argentine intelligence, Justice Minister Anibal Fernandez and others, arguing that the GoA action was an embarrassment and runs against Argentina's strategic interests. He said Anibal Fernandez quietly whispered in his ear that he agrees.

¶27. (C) Montoto said he is working hard to raise consciousness in Argentina and the region about the dangerous arms build-up by Venezuela which he believes emboldens Chavez to make bellicose statements against neighbors like Colombia.

He said this build-up also spurs similar purchases by Brazil. Meanwhile, Argentina's military is severely under-funded. This means that the United States is strategically more important than ever to Argentina, and the GoA should reinforce its defense dialogue and cooperation with the U.S., not limit it. He said he argues with GoA officials about this. He also said he had a very frank talk with former President Nestor Kirchner recently where he warned the ex-president about the inapplicability of Chavez' model for Argentina and about being careful not to become captive to Chavez. NK listened but did not concede the points, Montoto said.

¶28. (C) On public security, Montoto said he believes Argentines in greater Buenos Aires are going to judge their government on how well it controls crime and returns peace to the neighborhoods. This is the reason that Buenos Aires province governor Daniel Scioli, whom Montoto advises, has just rolled out a big effort to get more police on the streets: he wants to show his voters that he is acting boldly on this serious problem. Montoto said he just worked out the broad outlines of an agreement between the State of Rio de Janeiro and the Province of Buenos Aires to share experiences and expertise on public security. Montoto said he has told Scioli that he believes Buenos Aires may face the same serious problems as Rio in a couple of years if firm action is not taken now. Of course, the other part of the solution is job creation, and that is why Scioli is also taking a number of steps to promote SME creation and to attract investment, including from the United State.

Fund Manager, Entrepreneur, and Real Estate Magnate  
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¶29. (SBU) Eduardo Elsztain is the founder of Dolphin Fund Management (with several very large U.S. partners), President of IRSA Inversiones y Representaciones (real estate), and Cresud (livestock), among many other activities. He is an active civic leader and active in the NGO Endeavor which promotes young entrepreneurs.

¶30. (C) Elsztain argues that the key to understanding Argentine economic developments is to realize that it's the concrete that matters (e.g., real estate, not financial instruments). Right now, the key factor is salaries - how will the government negotiate new salary caps with the unions. Argentina is well-placed to weather current economic problems in the world. "I would rather have a populist government with a good fiscal policy and reserves, than a liberal government with a big deficit." But, it will be very important what policy signals the government sends to

investors. This government is on the right side of the  
""private property"" debate compared to Chavez, but it is not  
yet clear that it will come up with the right set of  
policies. If it does, plenty of capital will flow here.  
Essential to sustain such capital flows will be the justice  
system and sanctity of contracts. Elsztain noted that his  
investments in Brazil are currently valued three times higher  
than similar investments in Argentina in good part because  
people have more faith in the enforceability of contractual  
agreements in Brazil. Still, investments in solid things  
such as real estate and gold are good, and he will pursue  
some additional mining investments in Argentina, for example.  
(The strength of the Brazilian Real is also a factor in  
Brazilian values, he noted.)

¶31. (SBU) Elsztain said he had just donated a computer  
center for kids in the city of Buenos Aires with Mayor  
Mauricio Macri earlier in the week, and Macri had asked him  
to work on creating 90 more. Elsztain said he thought there  
was room to work with the U.S. Embassy on this project.

Oil Man and Entrepreneur  
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¶32. (C) Jorge Estrada is a Colombian-Argentine-American who  
started his career as a successful oilman and has  
subsequently branched out successfully in many other areas.  
In his view, inflation is the key issue facing the new  
government, with the real figure probably somewhere around  
18%. The government has been sending all the wrong signals  
to the oil and gas sector. At present, for example, wealthy  
households pay less for gas than do the poorest, who are  
compelled to pay world prices to buy bottled gas for their  
homes. While the government has been able to raise a lot of  
money through its export taxes, the result is that the price  
market does not work effectively, and production and  
investment are distorted in agriculture as well as oil and  
gas. The government should move to new taxing and pricing  
schemes, he opined; it could still collect more taxes via

income taxes rather than using the export taxes. Right now, the Argentine economy is well-placed to support such economic reforms. Demand for Argentina's commodities is high, and will remain so for a couple of years.

133. (C) At present, it is not yet clear that the government is ready to introduce significant reforms. Nestor Kirchner seems to still call many of the shots, and the government seems to function in the same way as it did when he was president. There is still no evident long-term vision. GOA reactions to events are often based on domestic political calculations, and there is little appreciation of other countries. All of this was evident in the reaction to the court case in Miami. As for the suitcase money itself, it was probably coming in for some under-the-table deal, he commented, but not likely for CFK's own campaign. She had plenty of campaign money flowing in from various sources in country, including the government.

134. (C) As for overall corruption, it seems as bad or worse than under Menem. In the oil area, two old friends of Nestor Kirchner have won many of the concessions offered publicly: the bidding rules were designed so they would win. Also, Nestor Kirchner has been a master at using state revenue to build alliances with governors and mayors. Kirchner has used his combative style (characteristically followed by a subsequent embrace) to build a set of alliances founded on mutual interests and fear. With Argentine supermarket owner Coto, for example, he first criticized him harshly, almost forced him to go broke, and then saved his business. Coto is now an ally.

WAYNE

=====CABLE ENDS=====